



Offshore funds – the Irish Dimension

An overview of Irish legal issues to be considered where an offshore fund is administered in Ireland

The key role Ireland plays as an administration and servicing hub for funds domiciled in offshore jurisdictions continues to grow. The latest industry figures show that an incredible 43 per cent of global hedge fund assets are now administered in Ireland. This amounts to some €987 billion held in over 6,000 non-Irish funds which together represent almost 50% of the total assets under administration in Ireland¹.

This article seeks to illustrate some of the Irish legal issues which arise for offshore structures taking advantage of this increasingly standard industry model for alternative products.

Background

The primary reason for Ireland's attractiveness as an international fund administration hub is the considerable body of local industry expertise which has been built up since the establishment of the International Financial Services Centre in Dublin in 1987. This expertise has included a particular focus on alternative investment products over the last ten years, and the clustering effect created by this accumulated know-how has seen the establishment of over 50 licensed fund administrators, including all of the big industry names as well as a host of smaller players and niche operators, which together give Ireland an unrivalled position as the leading jurisdiction for the administration of alternative assets.

Apart from having a significant number of personnel with specific fund administration expertise, as an English speaking, pro-business environment located in an optimum time zone to ensure global coverage, Ireland remains among the world's most attractive locations for general international business operations. It is rated in the top ten places in the world in which to do business by the World Bank and is consistently highly rated in the world's "best places to do business".

In addition, the recession in the general Irish economy since 2008 has proven a boost for the international financial services sector as it has driven down its cost base in terms of rent, labour and services while simultaneously increasing the availability of qualified staff and helped to improve service quality by dramatically reducing turnover among existing staff.

Administration

Fund administration is a regulated activity in Ireland and administration firms are generally authorised and supervised by the Irish financial regulator, the Central Bank of Ireland (the "Central Bank"), under the Investment Intermediaries Act 1995 (the "IIA"). This legislation applies to firms responsible for carrying on the administration of collective investment schemes, including the performance of valuation services or fund accounting services, as well as those acting as transfer agents or registration agents for such funds. Under the terms of this legislation, the Central Bank can determine the scope of services permitted to be

¹ Source: IFIA Statistics Factsheet, July 2011



provided and has to be satisfied as to the organisational structure of the administrator, as well as its conduct of business, the probity and competence of its directors and managers and a range of ancillary matters. The Central Bank may impose such conditions and requirements as it deems fit in order to ensure the proper regulation and supervision of the business and the protection of clients and investors.

Given that the conduct of the business of the administrator, as well as a wide variety of other aspects of its business, are subject to the requirements of the Central Bank this may have a practical impact on the scope of the regulated services provided or the manner of their provision.

In particular, the terms of administration agreements will generally require a representation from the administrator, that it has all necessary authorisations under local law and carries out its obligations under the contract in accordance with these. In this case this would typically mean the IIA and any powers the Central Bank had exercised under it or conditions it has imposed. Administration agreements with Irish based administrators are typically subject to Irish law and subject to an exclusive Irish jurisdiction clause also.

Data Protection

The Irish Data Protection Acts of 1988 and 2003 (together the “DPA”) provide for the statutory regime regulating the collection, storage, processing and treatment of personal data in Ireland. The DPA implement EU Data Protection Directive 95/46/EC on the protection of individuals with regard to the processing of personal data and on the free movement of such data. The Office of the Data Protection Commissioner is the Irish body responsible for upholding the rights of individuals as set out in the DPA and enforcing related obligations upon data controllers.

“Personal Data” is defined in the DPA as data relating to a living individual who is or can be identified either from the data or from the data in conjunction with other information that is in, or is likely to come into, the possession of the data controller. A “data controller” is defined to mean a person who, either alone or with others, controls the contents and use of personal data and a “data processor” means a person who processes personal data on behalf of a data controller but does not include an employee of a data controller who processes such data in the course of his employment.

Typically information provided by investors in the fund subscription process will constitute personal data for the purposes of the DPA and as such will be subject to its terms, with the fund itself constituting the data controller and the fund administrator being deemed to be the data processor. The general requirements imposed under the DPA are not onerous and are in broad terms similar to such laws across the European Union. However, it can be noted that there are particular requirements applicable where the relevant data constitutes “sensitive data”. This is defined to include, among other matters, personal data as to the racial or ethnic origin, the political opinion or the religious or philosophical beliefs of the data subject.

It is clear that this definition is sufficiently broad to encompass data which fund distributors might collect for marketing purposes - for example in relation to Sharia funds.

Apart from ensuring personal data is gathered, stored and treated in accordance with the relevant legal requirements it is appropriate to ensure that this issue is adequately addressed in relevant documents, including the funds’ subscription agreement with investors.

Anti-Money Laundering

Ireland, a member of the Financial Action Task Force (FATF), the EU and the OECD is a “white list” country for the purposes of anti-money laundering (“AML”) compliance. The Criminal Justice (Money Laundering and Terrorist Financing) Act 2010 was enacted into Irish law in July 2010 to update the existing Irish anti-money laundering and terrorist financing provisions contained in the Criminal Justice Act 1994 and the Criminal Justice (Terrorist Offences) Act, 2005 and bring them in line with the requirements of the EU’s Third AML Directive (Directive 60/2005/EC). Fund administrators carrying on business in Ireland constitute “designated persons” under the terms of this legislation and as such will be subject to it and obliged to carry out AML procedures in accordance with it.

It can be noted that Ireland’s AML regime is specifically recognised under the AML requirements of the Cayman Islands, being the Money Laundering Regulations (2009 Revision) (the “Regulations”). In addition the “Guidance Notes on the Prevention and Detection of Money Laundering in the Cayman Islands” issued by the Cayman Islands Monetary Authority in March 2010 specifically provide that Cayman funds can meet their AML obligations by delegating this function to a third party which is subject to the AML regime of certain countries, including Ireland, as specified in the third schedule to the Regulations.



In view of the foregoing it may make sense for offshore funds administered in Ireland to take advantage of the Irish AML regime and apply it when carrying out required AML procedures on behalf of the fund itself.

However, it should be noted that in such cases the relevant law in relation to the application of the AML procedures will, under Cayman law, be Irish law. Therefore where this route is being used it will be appropriate for the fund's administration agreement to contain an appropriate term delegating this role or acknowledging responsibility for the provision of this function. The subscription agreement with investors should also reflect this.

Listing

The Irish Stock Exchange (the "ISE") is the world's most popular exchange for the listing of investment funds and there are currently over 7,000 classes of shares of investment funds listed on it. The majority of offshore funds that are listed use the ISE for their listing.

The primary reasons for listing a fund are to increase a fund's potential investor base by providing access to institutional investors that are either restricted or prohibited from investing in unlisted securities or securities which are not listed on a recognised, regulated stock exchange, to enable the provision of a publicly quoted stock exchange price for shares, to increase a fund's prestige and profile and to provide a forum to offer publicly available information for investors.

The ISE has become the world's leading exchange for listing investment funds due to a range of factors including its reputation as a long established (est. 1793), well regulated and reputable European stock exchange, which has received the relevant recognitions from the market authorities in many jurisdictions including Japan and the United States. Having listed investment funds since 1989 the exchange has a wealth of experience regarding funds from almost every major fund domicile and since 1996 it has applied a specialised set of listing requirements for investment funds.

The ISE is authorised as a "market operator" of regulated markets and a multilateral trading facility by the Central Bank and as a result has certain regulatory responsibilities under Irish law, in particular to assess the eligibility of issuers and their securities for admission to official listing, both at the time of admission and on an on-going basis.

Consequently, the ISE requires issuers seeking admission of their securities to listing on the ISE's markets to comply with certain conditions both initially to obtain a listing and on an ongoing basis while the listing is maintained and in the case of investment funds this involves compliance with their "Listing Requirements & Procedures for Investment Funds", which have been specifically tailored for this sector and designed to ensure that Ireland has a well regulated, commercial and focussed listing regime.

As a listing on the ISE may require significant changes to a fund to comply with its requirements – for example structural amendments such as the appointment of a custodian, amendments to investment policy to comply with the applicable investment restrictions and new board members to ensure that there are independent directors – it is advisable for potential applicants to seek Irish advice on the requirements well in advance of a listing application.

Listing on the ISE will entail the appointment of an approved Listing Sponsor. This will be one of the nine approved Irish entities and the engagement agreement with this entity will be governed by Irish law.

Directors and Tax Issues

In view of the multiple connections outlined above it is very common for offshore funds, and particularly those listed on the ISE, to have Irish resident directors, even though there is no requirement in this regard for non-Irish funds.

The general rule under the Irish tax code (following the enactment of the Irish Finance Act 1999) is that a company incorporated in Ireland is, generally, to be treated as resident in Ireland for tax purposes, subject to a limited number of exceptions. However, while this legislation clarified the position somewhat in relation to Irish incorporated companies, it does not amend the existing position with regard to non-Irish incorporated corporates.

In such cases the question as to whether an entity is Irish resident is determined, in accordance with common law case law on the point, by the application of the "central management and control" test. The concept of a company's "central management and control" has been subject to judicial review and there is a significant body of common law case law on this area. A company's central management and control will be a matter of fact and the case law generally supports the contention that the place where the directors of the company meet is usually indicative of where central management and control is exercised and consequently where the company is resident.

Where Irish resident individuals act as directors on the boards of offshore funds care should naturally be taken in organising the corporate governance arrangements and carrying out effective control of the relevant corporate structure so as not to inadvertently trigger the Irish residency criteria because corporate entities resident in Ireland (other than investment funds duly authorised by the Central Bank, which are exempt) are subject to Irish corporation tax on their worldwide profits.

At the same time it can be noted that there may be advantageous considerations to deliberately intending the non-Irish incorporated company to be Irish tax resident. This may arise where it is intended to take advantage of the treaty benefits afforded to Irish resident companies under the double tax treaties which Ireland is a party to with over 60 countries, while simultaneously enjoying the lighter on-going corporate compliance requirements which may be applicable in offshore jurisdictions. Where a deliberate intention is being considered additional steps, such as nominating a registered office in Ireland etc., will typically be undertaken to strengthen the link with Ireland and provide greater certainty on this point.

Irish Courts

Given that in the event of a dispute in relation to many of the matters under discussion here the courts of Ireland are a likely choice of venue, and may indeed be the appropriate venue where there is an exclusive jurisdiction clause referencing Ireland, it would be appropriate to mention a relevant development in this regard. In 2004, the Minister for Justice announced the establishment of a specialist commercial division of the High Court to deal with an extensive range of commercial disputes, primarily involving claims with a value in excess of €1,000,000.

The primary aim of this development was to expedite commercial litigation proceedings in Ireland and to compel the parties to focus only on the specific issues in dispute. The new rules contain an extensive definition of the type of matters which may be considered to be "commercial" and this would include contractual matters relating to fund services. The definition also includes proceedings under the Arbitration Acts 1954 to 1998, which may be of relevance where the relevant contact has an arbitration clause, as is often the case in agreements relating to financial services especially where they are between institutional parties. The Commercial Court has resulted in proceedings that fall within its jurisdiction progressing significantly quicker than typical High Court proceedings and, in some cases, the entire process has taken less than 6 months.

In light of this, and the general convenience of Ireland for a large proportion of parties involved in fund disputes, Ireland will represent a preferred choice of jurisdiction for fund disputes in many cases and, in particular, it may be preferable to launching proceedings in an offshore jurisdiction.

Re-domiciling

In the light of the level of activities already performed in Ireland in relation to certain offshore vehicles, it may make sense to simply redomicile the structure to Ireland. Apart from the convenience of simplifying the number of jurisdictions involved in the structure there are numerous advantages to having an alternative fund domiciled in a tax efficient, on-shore, OECD and FATF member country like Ireland from the perspective of increasing the attractiveness of the structure to potential investors. In particular, it can be noted that from 2013 it should be possible for Irish Qualifying Investor Funds ("QIFs") to take advantage of the new pan European passport under the Alternative Investment Funds Management Directive and hence obtain access to superior distribution opportunities.

In addition it can be noted that the Central Bank has revised its requirements in relation to the QIF over the past 12 months in particular so that this vehicle, which is already the most popular structure for European hedge funds, with 63% of the market, now has very similar requirements to the standard Cayman fund, being a fund established under Section 4(3) of the Mutual Funds law (2009 revision). It is also typically more cost effective. As a result the proportion of global alternative assets held in Irish QIFs has doubled over the past 18 months.

Following the enactment of specific legislation in Ireland in late 2009 and the subsequent issuance of detailed guidance by the Central Bank, it is now possible to redomicile an existing offshore fund, whether structured in corporate or unincorporated form, to Ireland by means of a straightforward established procedure.

The key advantages of this redomiciliation process include the following:

- the existing legal identity of the migrating entity is retained;
- there is no need to incur the cost of establishing a new legal entity;
- there is no tax inefficient transfer of assets between funds;



- the fund authorisation by the Central Bank and the registration in Ireland take place simultaneously, accordingly the entity is exempt from tax as soon as the redomiciliation is effected; and
- the fund retains its existing contractual arrangements, its track record and its listing history.

Summary

Ireland is the world's leading servicing jurisdiction for offshore funds. However, when availing of administration, anti-money laundering or listing services from Irish entities for an offshore fund, it is appropriate to be cognisant of the implications of this under Irish law and this article gives an overview of some of the key points to be considered.

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Mark Browne is a Partner in the Financial Services Department of Mason Hayes+Curran specialising in Investment Funds.

Mark has over 10 years' experience in the funds industry and advises on all aspects of the structuring, establishment and ongoing operation of investment funds in Ireland, as well as in regard to issues affecting service providers such as administrators, custodians, distributors and investment managers.

Mark practised as an Attorney-at-Law specialising in hedge funds in the funds practice of a leading firm in the Cayman Islands for four years and advises on the redomiciliation of offshore funds to Ireland and the restructuring of hedge funds as UCITS. He previously worked in the investment funds department of another large Irish firm and for a leading global custodian in Luxembourg.

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